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In the Supreme Court of the United States

OCTOBER TERM, 1934

No. 10

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, petitioner

v.

STOCKHOLMS ENSKILDA BANK

ON A WRIT OF CERTIORARI TO THE COURT OF APPEALS OF THE DISTRICT OF COLUMBIA

BRIEF FOR THE PETITIONER

OPINIONS BELOW

The opinion of the Board of Tax Appeals (R. 8) is reported in 25 B.T.A. 1328. The opinion of the Court of Appeals of the District of Columbia (R. 19) is reported in 68 F. (2d) 407.

JURISDICTION

The judgment below was entered December 4, 1933. (R. 22.) On February 27, 1934, the Chief Justice entered an order granting an extension of time for the filing of a petition for a writ of cer-

tiorari for sixty days from March 4, 1934 (R. 23). The petition for a writ of certiorari was filed March 24, 1934, and was granted April 30, 1934. The jurisdiction of this Court rests on Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether interest paid during 1927 by the United States to a foreign corporation on a refund of taxes, pursuant to Section 1116 (a) of the Revenue Act of 1926, constitutes interest on an interest-bearing obligation of a resident, corporate or otherwise, within the meaning of Section 217 (a) (1) of the Revenue Act of 1926, made applicable in determining the gross income of a foreign corporation derived from sources within the United States by Section 233 (b) of that Act.

STATUTES INVOLVED

The statutes involved are set forth in the Appendix, *infra,* pp. 28–35.

STATEMENT

The facts are undisputed. As stated in the opinion of the Board of Tax Appeals, they are as follows (R. 8):

The respondent is a foreign corporation, organized and existing under the laws of the Kingdom of Sweden, with its principal office in that country. It has no office or place of business in the United

States. During the year 1927 the respondent received from the United States Government the sum of $8,683.91 as interest on a refund of Federal income taxes which had been overpaid for a prior year. The Commissioner of Internal Revenue increased the respondent's income for the year 1927 by including therein the interest on the refund, and on account of such increase determined a deficiency in the sum of $1,173.32. (See R. 4–5.) The respondent thereupon appealed to the Board of Tax Appeals (R. 2–3). That Board held that while the interest on the refund was interest on an interest-bearing obligation of the United States, the United States is not a "resident" within the meaning of Section 217 (a) (1) of the Revenue Act of 1926 which, taken in connection with Section 233 (b) of that Act, permits the inclusion in the gross income of a foreign corporation of "interest on bonds, notes, or other interest-bearing obligations of residents, corporate or otherwise." It therefore ruled that the Commissioner erred in including the interest on the refund in the respondent's gross income for the year 1927. (R. 8–11.) The Commissioner appealed to the Court of Appeals of the District of Columbia (R. 12–13), which affirmed the decision of the Board upon the same ground, one judge dissenting (R. 19–22).

SPECIFICATION OF ERRORS TO BE URGED

The Court of Appeals of the District of Columbia erred—

(1) In holding that the interest paid by the United States to the respondent upon the overpayment of its income taxes did not constitute interest on an interest-bearing obligation of a resident, corporate or otherwise, within the meaning of Section 217 (a) (1) of the Revenue Act of 1926, made applicable in determining the gross income of a foreign corporation derived from sources within the United States by Section 233 (b) of that Act.

(2) In sustaining the decision of the Board of Tax Appeals.

SUMMARY OF ARGUMENT

Section 233 (b) of the Revenue Act of 1926 provides that "In the case of a foreign corporation, gross income means only gross income from sources within the United States, determined * * * in the manner provided in section 217." Section 217 (a) (1) includes in the items of gross income to be treated as income from sources within the United States, "Interest on bonds, notes, or other interest-bearing obligations of residents, corporate or otherwise."

Section 217 when considered as a whole and in the light of its legislative history discloses a purpose on the part of Congress to tax all income received by a foreign corporation from sources within the United States except that expressly exempted. Interest upon an overpayment of Federal taxes is clearly income from a source within the United States. To accomplish the legislative purpose Sec-

tion 217 (a) (1) should be so construed as to require the inclusion in gross income of such interest when paid to a foreign corporation if the language of the section permits it. The language is sufficiently broad to achieve the Congressional aim. A contrary construction of the section would result in preferring the foreign corporation over the domestic corporation.

ARGUMENT

Section 3220 of the Revised Statutes, as amended by Section 1111 of the Revenue Act of 1926 (*infra*, p. 34), authorizes the Commissioner of Internal Revenue to "remit, refund, and pay back all taxes erroneously or illegally assessed or collected." Section 284 (a) of the Revenue Act of 1926 (*infra*, p. 33) provides that where there has been an overpayment of any income tax imposed under a prior revenue law "the amount of such overpayment shall * * * be credited against any income, war-profits, or excess-profits tax or installment thereof then due from the taxpayer, and any balance of such excess shall be refunded immediately to the taxpayer." Section 1116 (a) of the Revenue Act of 1926 (*infra*, p. 34) provides for the payment of interest at 6 percent upon the allowance of a credit or refund of any tax erroneously collected.

Pursuant to these statutes the United States refunded an overpayment of income tax made by the respondent some time prior to 1927. During 1927

the United States paid the respondent as interest on this refund the sum of $8,683.91. The question presented is whether this interest should be treated as a part of the respondent's gross income for the purpose of computing its income tax for 1927.

Section 233 (b) of the Revenue Act of 1926 (*infra*, p. 33), provides:

> In the case of a foreign corporation, gross income means only gross income from sources within the United States, determined * * * in the manner provided in section 217.

Section 217 (a) (1) (*infra*, p. 29) provides:

> In the case of a nonresident alien individual * * *, the following items of gross income shall be treated as income from sources within the United States:
>
> (1) Interest on bonds, notes, or other interest-bearing obligations of residents, corporate or otherwise, * * *.

Section 217 (c) (1) provides that:

> The following items of gross income shall be treated as income from sources without the United States:
>
> (1) Interest other than that derived from sources within the United States as provided in paragraph (1) of subdivision (a).

The Board of Tax Appeals held that the interest on the refund of taxes made to the respondent, although interest on an interest-bearing obligation of the United States was not interest on an interest-

bearing obligation of a "resident, corporate, or otherwise", because the United States was not a "resident" within the meaning of Section 217 (a) (1). The court below affirmed the decision of the Board upon the same ground. In the later case of *British-American Tobacco Co.* v. *Helvering, Commissioner,* involving the same question, which is now pending in this Court upon writ of certiorari (No. 24) and which is set for hearing with the instant case, while the Board reaffirmed its ruling in the present case (No. 24, R. 16), three members dissented, two of them writing opinions (No. 24, R. 17–24). One of the majority concurred in the result without writing an opinion (No. 24, R. 16), and another of the majority wrote a concurring opinion with which another of the majority agreed (No. 24, R. 16–17). In this concurring opinion the member disagreed with the Board in its holding that the Government of the United States was not a "resident" within the meaning of Section 217 (a) (1), but was of the opinion that as a refund of illegal taxes was not an "obligation of the United States" within the meaning of another provision of the Revenue Act of 1926, to which reference later will be made, it could not be considered such an "obligation" of the United States, even though the latter be deemed a "resident", as brought it within the scope of Section 217 (a) (1). Upon appeal the Circuit Court of Appeals for the

Second Circuit unanimously reversed the decision of the Board (No. 22, R. 32–38).

We believe that a careful analysis of Section 217, particularly when considered in the light of its legislative history, will disclose that the decision of the Circuit Court of Appeals for the Second Circuit was correct and that the decisions of the court below and the Board of Tax Appeals were incorrect. The pertinent portions of Section 217 are copied in the Appendix (*infra,* pp. 29–33). It will be observed that Congress in this section (made applicable in determining the gross income of a foreign corporation by Section 233 (b)) has divided the gross income of a foreign corporation into two groups, income from sources within the United States and income from sources without the United States. The items of gross income which are treated as income from sources within the United States are enumerated in subdivisions (a) and (e). Briefly stated they are, insofar as applicable to a foreign corporation rather than a nonresident alien individual, the class of taxpayers with which the section was primarily concerned: (1) interest on bonds, notes, or other interest-bearing obligations of a resident, corporate or otherwise; (2) amounts received as dividends from certain domestic corporations and from certain foreign corporations deriving a certain percentage of their income from sources within the United States; (3) "compensation for labor or personal serv-

ices performed in the United States", insofar, of course, as that phrase can be applied to a corporation; (4) rentals or royalties from property located in the United States; (5) gains and profits from the sale of real property located in the United States (subdivision (a)); and (6) items of gross income other than those specified in subdivisions (a) and (c), provision being made for the allocation of the income to sources within or without the United States under regulations to be prescribed by the Commissioner of Internal Revenue with the approval of the Secretary of the Treasury (subdivision (e)).[1] Considering these provisions as a whole, it is evident that Congress attempted to make a comprehensive statement of the various items of gross income which it was likely that a foreign corporation might derive from sources within the United States. That it intended this enumeration to be all-embracing is evident from the fact that where it desired to exclude from gross income items of income which normally would be considered as derived, either in whole or in part, from sources within the United States, it expressly

[1] It is evident from a reading of subdivision (e) that this subdivision covers items of income in respect of which difficulty is encountered in determining the proportion of the income which should be allocated to sources within the United States and the proportion which should be allocated ~~to sources without the United States, i.e., profit from trans-~~ to sources without the United States, i.e., profit from transportation or other services performed partly within and partly without the United States; profit from the sale of goods produced within and sold without the United States, etc.

said so. Thus, it said in subdivision (a) that interest on bonds, notes, or other interest-bearing obligations of a resident should not include interest on deposits with persons carrying on the banking business paid to persons not engaged in business within the United States and not having a place of business therein, or interest received from a resident alien individual, a resident foreign corporation, or a domestic corporation where it appears that the resident payor or the domestic corporation has derived less than 20% of its income from sources within the United States during the preceding three-year period, etc. Subdivision (c) (*infra,* p. 31), upon which the respondent relies, neither adds to nor detracts from the scope of the other provisions of the section. It is obviously complementary to subdivision (a) and merely says, in effect, that that which subdivision (a) does not include as gross income derived from sources within the United States shall be treated as coming from sources without the United States and therefore excluded from gross income.

From the very face of the section we think it is evident that it was the intent of Congress to require a foreign corporation to include in its gross income all items of income derived from sources within the United States unless excluded by express language. That such was the intent of Congress is made further manifest when the legislative history of the section is considered.

The Tariff Act of October 3, 1913, c. 16, 38 Stat. 114, 172, provided in Section II G (a) for the levy of a tax upon the net income of foreign corporations, the same to include "the amount of net income accruing from business transacted and capital invested within the United States during such year." In response to a question from the Secretary of the Treasury on August 24, 1915, the Attorney General held (30 Op.A.G. 435) that under the Act of 1913 a foreign corporation was exempt from tax on income derived from stocks or bonds of domestic corporations doing a domestic business, or from obligations secured by mortgages on tangible property within the United States, even though such obligations were held by such foreign corporation in the United States.

The Revenue Act of 1916, c. 463, 39 Stat. 756, 765, enacted September 8, 1916, sought to correct this situation. Section 10 of that Act provided that

> a like tax shall be levied, assessed, collected, and paid annually upon the total net income received in the preceding calendar year *from all sources within the United States* by every corporation * * * authorized, or existing under the laws of any foreign country, *including interest on bonds, notes, or other interest-bearing obligations of residents, corporate or otherwise.* * * *. (Italics ours.)

It will at once be seen that in the 1916 Act Congress not only sought to make the test of taxability

of foreign corporations the "source" of the income,[2] but it definitely had in mind the ruling of the Attorney General, *supra,* and therefore specifically inserted the phrase "including interest on bonds, notes, or other interest-bearing obligations of residents, corporate or otherwise." It is evident, therefore, that this last phrase was not intended in any wise to restrict the scope of the section. Its primary purpose was patently a precautionary one of insuring that this type of income, received unquestionably from a source within the United States, should not in the future be held to be excluded from taxable income.

The provisions of Section 10 of the Revenue Act of 1916 were carried forward without substantial change into Section 233 (b) of the Revenue Act of 1918, c. 18, 40 Stat. 1057, 1077.

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[2] In Holmes, Federal Taxes, 6th ed., Sec. 204, p. 397, it is said:

"The intention of Congress in the 1916 and subsequent statutes seems to have been to discard the 1909 and 1913 basis of taxing nonresident aliens and foreign corporations and to make the test of taxability the "source" or situs of the activities or property which produce the income or from which it is desired [derived]. The result is that, on the one hand, nonresident alien and foreign corporations are prevented from deriving income from the United States free from tax by virtue of a technical construction of the phrase, "property owned * * * and * * * business, trade or profession carried on" and the phrase "business transacted and capital invested"; and, on the other hand, there is no undue imposition of a tax when the activities and property producing the income do not take place or is not employed in this country."

In enacting this legislation, Congress undoubtedly thought that it was laying the foundation for taxing all income derived *from sources within the United States.* However, subsequent to the enactment of the 1918 Act, difficult administrative questions began to arise. On August 12, 1920, the Secretary of the Treasury submitted to the Attorney General several questions with reference to the source from which certain designated incomes had been derived. In an opinion dated November 3, 1920, the Attorney General, among other things, held (32 Op. A. G. 336):

> (1) That a foreign corporation partially manufacturing articles in this country, shipping them to England, finishing them and selling them there, derived no income from sources within the United States, within the meaning of the above Acts;
>
> (2) That income accruing to a foreign corporation from the purchase of logs in this country and their sale abroad did not constitute income from sources within the United States;
>
> (3) That income derived by a foreign corporation from the purchase of goods abroad and their sale in the United States through the medium of a New York corporation constituted income derived from sources within the United States; and
>
> (4) That income derived by a foreign steamship company from the transportation of freight and passengers from the United

> States to foreign ports constitutes income derived from sources within the United States.

This ruling brought forth many protests, with the result that Congress sought to remedy the situation. Hence, when H.R 8245, which later became the Revenue Act of 1921, c. 136, 42 Stat. 227, was being considered, the definition of gross income, so far as it related to foreign corporations, was incorporated in Sections 217 and 233 in the form subsequently carried forward into the Revenue Acts of 1924 (c. 234, 43 Stat. 253) and 1926. As to the Congressional purpose in making the change from the provisions of Section 233 (b) of the Revenue Act of 1918, the Committee on Finance of the Senate, in Report No. 275, 67th Cong., 1st Sess., p. 16, said:

> Section 217 states explicit rules—applicable principally to nonresident aliens and foreign traders—for computing the net income derived from sources within the United States. The present law is both obscure and economically unsound, inasmuch as the Attorney General has held that where goods are manufactured or produced in the United States and sold abroad, no part of the profit is derived from a source within the United States This section explicitly allocates certain important sources of income to the United States or to foreign countries, as the case may be, and with respect to the remaining income (particularly

> that derived partly from sources within and partly from sources without the United States) authorizes the commissioner, with the approval of the Secretary, to determine the income derived from sources within the United States either by rules of separate allocation or by processes or formulas of general apportionment.

Thus it will be seen that the history of the statute involved clearly indicates a purpose on the part of Congress to extend and make all-inclusive taxes upon the income of foreign corporations *derived from sources within the United States.* By making a comprehensive specification of the various items of income which a foreign corporation would normally derive from sources within the United States, Congress evidently thought that it could better accomplish its purpose and avoid the disputes which had arisen in the past through the use of general language. Congress certainly had no idea that it was not covering the whole field, for, as we have heretofore pointed out, where it desired for some reason to exclude a particular item of gross income which would otherwise normally have been deemed to have come from a source within the United States, it excluded such item from gross income by express language.

There can be no question from the standpoint of logic and of fact that interest paid by the United States Government to a foreign corporation upon a refund of taxes comes from a source within the

United States. The statute and its legislative history manifest the purpose of Congress to include all forms of income derived from sources within this country, unless expressly exempted. It has been held that interest on a tax refund when paid to an American corporation is not exempt under other provisions of the statute. *American Viscose Corporation* v. *Commissioner,* 56 F. (2d) 1033 (C.C.A. 3d), certiorari denied, 287 U.S. 615. To attribute to Congress the purpose to exempt similar income when paid to a foreign corporation is not only contrary to the recognized Congressional disposition to extend income taxes to all forms of taxable income (*Eisner* v. *Macomber,* 252 U.S. 189, 203; *Irwin* v. *Gavit,* 268 U.S. 161, 166; *Heiner* v. *Colonial Trust Co.,* 275 U.S. 232, 235), but also to the general nationalistic disposition to favor domestic corporations which expend their incomes in the United States.[3] Taxation being the rule and exemption the exception, any doubt is to be resolved in favor of taxation. *Bank of Commerce* v. *Tennessee,* 161 U.S. 134, 146; *Heiner* v. *Colonial Trust Co., supra; United States Trust Co. of New York* v. *Anderson,* 65 F. (2d) 575, 577 (C.C.A. 2d), certiorari denied, 290 U.S. 683. Except in the presence of clear and unmistakable language, it is hardly conceivable that Congress intended that the foreign

[3] For evidence of this disposition see the history of the Act of August 5, 1861, c. 45, 12 Stat. 292, 309, Sec. 49, as set forth in 30 Op.A.G. 437.

corporation should be favored over the domestic corporation, particularly where, as in the *British-American Tobacco* case, the foreign corporation is engaged in active competition in this country with American industry.

As is apparent from the face of the statute and its legislative history, the aim of the statute was to cover all forms of income accruing to a foreign corporation from sources within this country unless expressly exempted. The statute should accordingly be so construed "as to achieve, and not defeat, its aim." *Burnet* v. *Chicago Portrait Co.*, 285 U.S. 1, 7. Interest on a refund of Federal taxes is undoubtedly income arising from a source within the United States. There is apparent no logical reason for exempting such interest and it should be included in the gross income of the foreign corporation if the words of the statute, reasonably construed in the light of its manifest purpose, permit it. Section 217 (a) (1) provides that the following item of the gross income of a foreign corporation shall be treated as income coming from a source within the United States: "Interest on bonds, notes, or other interest-bearing obligations of a resident, corporate or otherwise." There can be little question that the interest received on a tax refund is interest on an interest-bearing obligation of the United States. In fact, only one of the various opinions in this and the *British-American Tobacco Co.* case questioned this, and that opinion was

influenced by the interpretation which had been given by one of the Circuit Courts of Appeals to the phrase "obligations of the United States" as used in another section of the Act, where, however, as will be explained later, the phrase was obviously employed as referring to obligations of the United States incurred in the borrowing of money. Section 284 (a) of the Revenue Act of 1926 (*infra*, p. 33) and Section 3220 of the Revised Statutes, as amended by Section 1111 of the Revenue Act of 1926 (*infra*, p. 34) make it the duty of the Commissioner of Internal Revenue to refund all taxes erroneously or illegally collected. That this statutory requirement constitutes an "obligation" of the United States within the ordinary meaning of that term is apparent. Webster's New International Dictionary defines the term "obligation" as including "any duty imposed by law." It is well settled that the popular and accepted import of words furnishes the general rule for the interpretation of public laws (*Woolford Realty Co.* v. *Rose*, 286 U.S. 319, 327; *Old Colony R. Co.* v. *Commissioner*, 284 U.S. 552, 560) unless it is clear that Congress used the word in a narrower sense (*United States* v. *First National Bank*, 234 U.S. 245, 258). The purpose of the section, as reflected in its terms and in its legislative history, refutes the idea that Congress intended that the word "obligations" should be used in a narrow sense.

While it is contended in the brief in opposition to the Government's petition in this case that the word "obligations" should be limited to obligations generically similar to bonds and notes, pursuant to the doctrine of *ejusdem generis,* the very language of the section discloses that this doctrine cannot be applied. After providing that there shall be included in the gross income of the foreign corporation interest on bonds, notes, or other interest-bearing obligations of a resident, the section specifically states that this interest shall not include "(A) interest on deposits with persons carrying on the banking business paid to persons not engaged in business within the United States and not having an office or place of business therein." It is obvious, as was held by the Board of Tax Appeals (R. 10), that Congress thought that "interest on deposits" with persons carrying on a banking business would have been included among "other interest-bearing obligations" had it not been specifically excluded, for otherwise there would have been no reason for the exclusion. *United States* v. *Woodward,* 256 U.S. 632, 634; *Brown* v. *Maryland,* 12 Wheat. 419, 438. Manifestly, "interest on deposits" is no more of a kind generically similar to bonds and notes than is interest on a statutory obligation of the United States.

If, as we contend, the doctrine of *ejusdem generis* does not apply, there obviously is no foundation for the further contention of the respondent

that the word "obligations" is confined to contractual as contrasted with statutory obligations. There is not a word in the section which leads to any such inference, and such a construction would be contrary to the manifest purpose of the statute.

If, as seems clear, the statutory duty and undertaking of the United States to refund an overpayment of income taxes is an "obligation" within the meaning of Section 217 (a) (1), there certainly can be no question that it is an "interest-bearing obligation." Section 1116 (a) of the Revenue Act of 1926 (*infra*, p. 34) specifically provides that interest shall be allowed at the rate of 6 per centum per annum on a refund of taxes from the date the taxes are paid to the date of the allowance of the refund.

We pass, then, to the only question as to which there was any serious controversy below either in the instant case or in the *British-American Tobacco Co.* case. Section 217 (a) (1) requires that the obligation shall be that of a "resident, corporate or otherwise." The Board of Tax Appeals in the instant case and in the *British-American Tobacco Co.* case and the court below in the instant case held that the United States could not be considered as a "resident" within the meaning of the section. The Circuit Court of Appeals for the Second Circuit in the *British-American Tobacco Co.* case, as well as five of the members of the Board of Tax Appeals, entertained a contrary view. Having in

mind the aim of Section 217 to include within its ambit all of the income of a foreign corporation derived from sources within this country unless expressly excepted, we submit that it is a permissible construction to hold that the United States is a "resident" within the meaning of the section. The section extends without qualification to corporate "residents", as well as individual residents. The language is sufficiently broad, as was said by the Circuit Court of Appeals for the Second Circuit in the *British-American Tobacco Co.* case, "to embrace all conceivable entities, be they sovereign, corporate, or individual." (No. 24, R. 35.) That the United States is a corporation can hardly be disputed. *United States* v. *Maurice*, 2 Brock. (U.S.) 96, 109 (per Marshal, C.J.); *Respublica* v. *Sweers*, 1 Dall. 41, 44. As was said by this Court in *Van Brocklin* v. *Tennessee*, 117 U.S. 151, 154, quoting from the language of Chief Justice Marshall in the *Maurice* case:

> The United States is a government, and consequently a body politic and corporate, capable of attaining the objects for which it was created, by the means which are necessary for their attainment. This great corporation was ordained and established by the American people, and endowed by them with great powers for important purposes. * * *

SEE ALSO OHIO v. HELVERING, 292 U.S. 360, 370.

As a corporate entity, the United States obviously must have a corporate residence somewhere.

While it cannot be said to reside at any particular place within its boundaries, being ubiquitous its corporate residence is obviously coterminous with its territorial limits. Cf. *United States* v. *Borcherling,* 185 U.S. 223, 233; *Mackey* v. *Coxe,* 18 How. 100, 105; *Wyman* v. *Halstead,* 109 U.S. 654. "If," as was said by one of the members of the Board of Tax Appeals in the *British-American Tobacco Co.* case, "the United States is not a 'resident' of the United States within the contemplation of the statute, of what country is it a 'resident'?" (No. 24, R. 19.) There can be no question that a sovereign resides where it is sovereign.

The only court decision upon which the court below relied in holding that the United States could not be considered a "resident" within the meaning of Section 217 is *State* v. *City of Trenton,* 40 N.J.L. 89. We do not think that that decision when properly analyzed supports the court's conclusion. Indeed, it applied the rule of construction which we believe is the proper one to apply in the present case. The law of New Jersey provided for the taxation of all real and personal property at its full and actual value, but allowed a deduction of debts due and owing to "creditors *residing* within the state." (Italics ours.) The taxpayer sought to deduct a debt owing to the State of New Jersey, and the question presented was whether the State was a *resident.* The court held that since the taxpayer was seeking an exemption from taxation a strict construction was required, and that, looking

to the purpose of the legislature in passing the law, it was clear that it intended to allow a deduction of a debt only where the person to whom the debt was owing would be required to include such debt in his personal property for the purpose of taxation. The court said (p. 92):

> If it was the intention to exempt the borrower of state funds from taxation to the amount of his loan, and withdraw from the taxable property of the state the large sum represented by the school fund, there should have been some clear expression of such purpose, and it should not be left to doubtful interpretation. When money passes out of the state treasury into the hands of a citizen, it loses its immunity from taxation as public funds, and becomes assessable as individual property, unless expressly exempted. The bonds and mortgages representing these funds are held by public officers as public property, and are not liable to taxation. Neither in the words used in this act nor in its reason, do I find the unambiguous expression which is required to exempt property from the burden of general taxation.

It is evident that the State court in this case did exactly what we contend the court below should have done—it first inquired into the primary purpose of the statute and then proceeded to interpret and apply its provisions in the light of the underlying purpose. Instead, the court below in the instant case gave no consideration to the purpose of the statute involved and resorted to a rule of strict con-

struction which had the effect of thwarting the intent of Congress as manifested not only in the statute itself but through its legislative history.

In reaching its decision the court below was, as is evident from its opinion, influenced to a considerable extent by the injustice which it seemed to think would result if the tax were sustained. After pointing out that "the payment in question represented interest which the Government was paying as provided by statute because of an overassessment of income taxes theretofore imposed by the Government upon the taxpayer," the court said that "To assess income taxes upon such a repayment would amount to the imposition of a penalty upon the taxpayer because of the error theretofore committed by the Government against him" (R. 21). As we have heretofore pointed out, a domestic corporation is not exempt from the payment of an income tax upon interest received on a refund of Federal taxes (*supra*, p. 16), and it is hardly likely that Congress would be more solicitous of the welfare of the foreign corporation, which uses its income abroad, than it would be of the domestic corporation, which spends its money in this country. There is no conceivable reason, so far as we can see, why Congress should have desired in the case of a foreign corporation to add to the high rate of interest allowed on tax refunds (6%).[4] Moreover,

[4] Allowed by Section 1324 (a) of the Revenue Act of 1921, Sections 1019 of the 1924 Act, and 1116 (a) of the Revenue Act of 1926.

the alleged injustice which the court feared would result from the taxation of interest on tax refunds made to foreign corporations is largely minimized when we consider some of the evils which might flow from a contrary decision. As was pointed out by one of the dissenting members of the Board of Tax Appeals in the *British-American Tobacco Co.* case (No. 24, R. 23–24):

> The possibilities of a tax-free yield of 6 percent to foreign corporations and nonresident aliens, which the decision in the Stockholms Bank case opens up, will not be overlooked, particularly by resident foreign corporations. Under our system of self-assessment, there is nothing to prevent such corporations from including in the return of income and paying income tax on items of foreign income or, even for that matter, tax-exempt income from United States sources, such as interest on Liberty Bonds and municipal bonds, knowing full well that a claim for refund filed within the statutory period, two years, based on the erroneous inclusion in gross income of items of income from sources without the United States and items of tax-exempt income, will be allowed and that the amount of such refund will draw interest at the rate of 6 percent from the date the tax was paid to the date of the allowance. The statute does not now require that the tax be paid under protest in order to obtain a refund.

It has been suggested that if it should be held that interest on a refund to a foreign corporation of

Federal taxes may be considered as interest on an "obligation" within the meaning of Section 217 (a) (1), the dilemma will be presented that the effect of such a decision will be to exempt this interest from taxation under Sections 213 (b) (4) (*infra,* p. 28) and 236 (a) (*infra,* p. 33). The dilemma is, we submit, purely mythical. The legislative history showing the relationship between the two sections is set forth at length in the opinion of the Circuit Court of Appeals in the *British-American Tobacco Co.* case and, therefore, need not be here repeated (No. 24, R. 37). A mere glance at Section 213 (b) (4) will disclose that it was the intention of Congress in the sections in question to deal only with obligations of the ~~State and~~ Federal Governments incurred in the borrowing of money. As was said by the Circuit Court of Appeals for the Third Circuit in the *American Viscose* case, *supra* (56 F. (2d) 1034), in holding that interest on a tax refund made to a domestic corporation was not exempted from taxation by Section 213 (b) (4):

> The exemptions of Congress were evidently meant to aid in the flotation of government bonds and securities by making them tax free and, therefore, more attractive to investors.

See also *United States Trust Co. of New York* v. *Anderson,* 65 F. (2d) 575 (C.C.A. 2d), a decision by the same Circuit Court of Appeals which decided the *British-American Tobacco Co.* case.

The meaning to be attributed to a particular word depends, of course, upon the intent with which it was used. In Sections 213 and 236 the legislative history and the language employed disclose that Congress intended that the word "obligations" should be given a narrow, restricted meaning. In the section with which we are concerned, it was the manifest intention of Congress to tax to foreign corporations all income derived from sources within the United States unless expressly excepted. To give to the word "obligations" as there used the limited meaning which was ascribed to it by the court below and by the Board of Tax Appeals is not to achieve but to defeat the aim of Congress.

CONCLUSION

For the reasons stated, we respectfully submit that the judgment below should be reversed.

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SEPTEMBER 1934.

APPENDIX

STATUTES INVOLVED

Revenue Act of 1926, c. 27, 44 Stat. 9:

SEC. 2. (a) When used in this Act—

* * * * * * *

(3) The term "domestic" when applied to a corporation or partnership means created or organized in the United States or under the law of the United States or of any State or Territory.

(4) The term "foreign" when applied to a corporation or partnership means a corporation or partnership which is not domestic.

(U.S.C.App., Title 26, Sec. 1262.)

SEC. 213. For the purposes of this title, except as otherwise provided in section 233—

(a) The term "gross income" includes * * *.

(b) The term "gross income" does not include the following items, which shall be exempt from taxation under this title:

* * * * *

(4) Interest upon (A) the obligations of a State, Territory, or any political subdivision thereof, or the District of Columbia; or (B) securities issued under the provisions of the Federal Farm Loan Act, or under the provisions of such Act as amended; or (C) the obligations of the United States or its possessions. Every person owning any of the obligations or securities enumerated in clause (A), (B), or (C) shall, in the return required by this title, submit a statement showing the

number and amount of such obligations and securities owned by him and the income received therefrom, in such form and with such information as the Commissioner may require. In the case of obligations of the United States issued after September 1, 1917 (other than postal-savings certificates of deposit), the interest shall be exempt only if and to the extent provided in the respective Acts authorizing the issue thereof as amended and supplemented, and shall be excluded from gross income only if and to the extent it is wholly exempt to the taxpayer from income taxes;

* * * * * * *

(U.S.C.App., Title 26, Sec. 954.)

SEC. 217. (a) In the case of a nonresident alien individual * * *, the following items of gross income shall be treated as income from sources within the United States:

(1) Interest on bonds, notes, or other interest-bearing obligations of residents, corporate or otherwise, not including (A) interest on deposits with persons carrying on the banking business paid to persons not engaged in business within the United States and not having an office or place of business therein, or (B) interest received from a resident alien individual, a resident foreign corporation, or a domestic corporation, when it is shown to the satisfaction of the Commissioner that less than 20 per centum of the gross income of such resident payor or domestic corporation has been derived from sources within the United States, as determined under the provisions of this section, for the three-year period ending with the close of the taxable year of such payor preceding the payment

of such interest, or for such part of such period as may be applicable;

(2) The amount received as dividends (A) from a domestic corporation other than a corporation entitled to the benefits of section 262, and other than a corporation less than 20 per centum of whose gross income is shown to the satisfaction of the Commissioner to have been derived from sources within the United States, as determined under the provisions of this section, for the three-year period ending with the close of the taxable year of such corporation preceding the declaration of such dividends (or for such part of such period as the corporation has been in existence), or (B) from a foreign corporation unless less than 50 per centum of the gross income of such foreign corporation for the three-year period ending with the close of its taxable year preceding the declaration of such dividends (or for such part of such period as the corporation has been in existence) was derived from sources within the United States as determined under the provisions of this section;

(3) Compensation for labor or personal services performed in the United States;

(4) Rentals or royalties from property located in the United States or from any interest in such property, including rentals or royalties for the use of or for the privilege of using in the United States, patents, copyrights, secret processes and formulas, good will, trade-marks, trade brands, franchises, and other like property; and

(5) Gains, profits, and income from the sale of real property located in the United States.

* * * * *

(c) The following items of gross income shall be treated as income from sources without the United States:

(1) Interest other than that derived from sources within the United States as provided in paragraph (1) of subdivision (a);

(2) Dividends other than those derived from sources within the United States as provided in paragraph (2) of subdivision (a);

(3) Compensation for labor or personal services performed without the United States;

(4) Rentals or royalties from property located without the United States or from any interest in such property, including rentals or royalties for the use of or for the privilege of using without the United States, patents, copyrights, secret processes and formulas, goodwill, trade marks, trade brands, franchises, and other like properties; and

(5) Gains, profits, and income from the sale of real property located without the United States.

* * * * * * *

(e) Items of gross income, expenses, losses and deductions, other than those specified in subdivisions (a) and (c), shall be allocated or apportioned to sources within or without the United States under rules and regulations prescribed by the Commissioner with the approval of the Secretary. Where items of gross income are separately allocated to sources within the United States, there shall be deducted (for the purpose of computing the net income therefrom) the expenses, losses, and other deductions properly apportioned or allocated thereto and a ratable part of other expenses, losses, or other deductions which cannot definitely be al-

located to some item or class of gross income. The remainder, if any, shall be included in full as net income from sources within the United States. In the case of gross income derived from sources partly within and partly without the United States, the net income may first be computed by deducting the expenses, losses, or other deductions apportioned or allocated thereto and a ratable part of any expenses, losses, or other deductions which cannot definitely be allocated to some items or class of gross income; and the portion of such net income attributable to sources within the United States may be determined by processes or formulas of general apportionment prescribed by the Commissioner with the approval of the Secretary. Gains, profits, and income from (1) transportation or other services rendered partly within and partly without the United States, or (2) from the sale of personal property produced (in whole or in part) by the taxpayer within and sold without the United States, or produced (in whole or in part) by the taxpayer without and sold within the United States, shall be treated as derived partly from sources within and partly from sources without the United States. Gains, profits, and income derived from the purchase of personal property within and its sale without the United States or from the purchase of personal property without and its sale within the United States, shall be treated as derived entirely from sources within the country in which sold, except that gains, profits, and income derived from the purchase of personal property within the United States and its sale within a possession of the United States or from the purchase of personal property within a possession of the United States

and its sale within the United States shall be treated as derived partly from sources within and partly from sources without the United States.

(U.S.C.App., Title 26, Sec. 958.)

SEC. 233. (a) In the case of a corporation subject to the tax imposed by section 230 the term "gross income" means the gross income as defined in sections 213 and 217, except that mutual marine insurance companies shall include in gross income the gross premiums collected and received by them less amounts paid for reinsurance.

(b) In the case of a foreign corporation, gross income means only gross income from sources within the United States, determined (except in the case of insurance companies subject to the tax imposed by sections 243 or 246) in the manner provided in section 217.

(U.S.C.App., Title 26, Sec. 985.)

SEC. 236. For the purpose only of the tax imposed by section 230 there shall be allowed the following credits:

(a) The amount received as interest upon obligations of the United States which is included in gross income under section 233; * * *.

(U.S.C.App., Title 26, Sec. 988.)

SEC. 284. (a) Where there has been an overpayment of any income, war-profits, or excess-profits tax imposed by this Act, the Act entitled "An Act to provide revenue, equalize duties, and encourage the industries of the United States, and for other purposes", approved August 5, 1909, the Act entitled "An Act to reduce tariff duties and to provide revenue for the Government, and for other purposes", approved October 3, 1913, the Revenue Act of 1916, the Revenue Act of 1917, the Revenue

Act of 1918, the Revenue Act of 1921, or the Revenue Act of 1924, or any such Act as amended, the amount of such overpayment shall, except as provided in subdivision (d), be credited against any income, war-profits, or excess-profits tax or installment thereof then due from the taxpayer, and any balance of such excess shall be refunded immediately to the taxpayer.

(U.S.C.App., Title 26, Sec. 1065.)

* * * * * * *

SEC. 1111. Section 3220 of the Revised Statutes, as amended, is amended to read as follows:

"SEC. 3220. Except as otherwise provided in sections 284 and 319 of the Revenue Act of 1926, the Commissioner of Internal Revenue, subject to regulations prescribed by the Secretary of the Treasury, is authorized to remit, refund, and pay back all taxes erroneously or illegally assessed or collected, all penalties collected without authority, and all taxes that appear to be unjustly assessed or excessive in amount, or in any manner wrongfully collected; also to repay to any collector or deputy collector the full amount of such sums of money as may be recovered against him in any court, for any internal-revenue taxes collected by him, with the cost and expenses of suit: * * *.

(U.S.C.App., Title 26, Sec. 149.)

SEC. 1116. (a) Upon the allowance of a credit or refund of any internal-revenue tax erroneously or illegally assessed or collected, or of any penalty collected without authority, or of any sum which was excessive or in any manner wrongfully collected, interest shall be allowed and paid on the amount of such credit or refund at the rate of 6 per centum per

annum from the date such tax, penalty, or sum was paid to the date of the allowance of the refund, or in the case of a credit, to the due date of the amount against which the credit is taken, but if the amount against which the credit is taken is an additional assessment made under the Revenue Act of 1921, the Revenue Act of 1924, or this Act, then to the date of the assessment of that amount.

(U.S.C.App., Title 26, Sec. 153.)

U. S. GOVERNMENT PRINTING OFFICE: 1934